

# BANKER & TRADESMAN

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## RESIDENTIAL REAL ESTATE

GUEST COMMENTARY

### First Circuit To Seek SJC Help On Bankruptcy Trustee 'Loophole' To Avoid Mortgages

SJC Expected To Provide Guidance In *Casey* Appeal

BY JASON A. MANEKAS  
SPECIAL TO BANKER & TRADESMAN

In connection with the subprime mortgage crisis, it was inescapable that borrowers would mount a litany of legal challenges to not only halt the foreclosures of their homes, but to also attack the validity of the underlying mortgages.



JASON MANEKAS

If all else failed, borrowers could file for bankruptcy protection, which will automatically "stay" the foreclosure sale, and avail themselves of the bankruptcy court's debtor-friendly protections.

Seizing upon that body of law, bankruptcy trustees mounted a new legal challenge seeking to permit debtor-borrowers to avoid their mortgages under the trustee's so-called "strong-arm powers" under Section 544(a) of the United States Bankruptcy Code. In essence, Section 544 empowers the trustee to avoid a transfer of an interest in real property of the debtor to the extent any bona fide purchaser may avoid the transfer. If the trustee is successful in his or her attempt to avoid the mortgage, the lender becomes an unsecured creditor and cannot foreclose upon

the property. In addition, the equity in the home will be available to pay unsecured creditors, to pay the trustee's fees, and, if the debtor-borrower claimed a homestead exemption, for the benefit of the debtor-borrower.

Thus, while a debtor-borrower who admittedly signed and acknowledged his/her mortgage cannot deny notice of its existence, a recent series of Massachusetts bankruptcy court rulings have allowed trustees to successfully challenge the enforcement of mortgages in which the certificate of acknowledgement is imperfect because of vague wording or a careless omission on a pre-printed form. The certificate of acknowledgement is the certificate of the notary public, justice of the peace or other authorized officer, attached to the mortgage setting forth that the parties thereto personally appeared before him/her on that particular date and acknowledged the instrument to be their free and voluntary act and deed.

However, a recent Massachusetts federal court decision, *Bank of Am., N.A. v. Casey*, rejected the trustee's challenge and upheld the validity of a mortgage in which a flawed certificate of acknowledgement was later corrected by an affidavit recorded in the registry of deeds. The *Casey* ruling not only allows a lender to cure the purported defect, but is a direct challenge to the so-

called *Giroux* line of decisions that allow bankruptcy trustees to avoid such mortgages altogether.

Now, the U.S. Court of Appeals for the First Circuit is hearing an appeal of *Casey* and is likely to certify questions to the Massachusetts Supreme Judicial Court (SJC) requesting guidance. Such a ruling by the SJC could profoundly affect the commonwealth's land recordation requirements and close a bankruptcy loophole that allows a trustee to deny constructive notice of a mortgage recorded at the registry of deeds even though the debtor-borrower admits to signing it, admits to acknowledging it before a notary, and lists it as a debt on his/her bankruptcy schedules.

The First Circuit heard oral arguments in *Casey* in early June 2015, and later this month is expected to certify questions to the SJC on the matter. Once the certification order is issued, the matter would be docketed, briefed and argued in the Massachusetts high court. While the SJC has discretion as to what questions it will ultimately answer, it is anticipated it will provide guidance to the federal courts and determine whether trustees can take advantage of this claimed loophole. ■

*Jason A. Manekas is a real estate litigation and business litigation partner at Bernkopf Goodman LLP.*